



Employees' Retirement Board of Rhode Island
Monthly Meeting Minutes
Wednesday, November 13, 2013
9:00 a.m.
2nd Floor Conference Room, 50 Service Avenue

The Monthly Meeting of the Retirement Board was called to order at 9:04 a.m. Wednesday, November 13, 2013, in the 2nd Floor Conference Room, 50 Service Avenue, Warwick, RI.

I. Roll Call of Members

The following members were present at roll call: Vice Chair William B. Finelli; Gary R. Alger, Esq.; Daniel L. Beardsley; Frank R. Benell, Jr.; Michael R. Boyce; M. Carl Heintzelman; Richard A. Licht; John P. Maguire; John J. Meehan; Thomas A. Mullaney; Claire M. Newell and Jean Rondeau.

Also in attendance: Frank J. Karpinski, ERSRI Executive Director; Attorney Michael P. Robinson, Board Counsel.

Recognizing a quorum, Vice Chairman Finelli called the meeting to order.

General Treasurer Gina M. Raimondo arrived at 9:10 a.m.

II. Approval of Minutes

On a motion by M. Carl Heintzelman and seconded by Frank R. Benell, Jr., it was unanimously

VOTED: To approve the draft minutes of the October 9, 2013 meeting of the Employees' Retirement System of Rhode Island.

III. Chairperson's Report

Treasurer Raimondo informed the Board there has been no update on the pension reform litigation.

The Treasurer then called Chief Investment Officer Anne-Marie Fink to provide an update on investments for the last quarter. Ms. Fink asked the Board to refer to the SIC Report provided in the board book. She noted that the quarter referenced is July 2013 to September 2013.

Ms. Fink said equity markets were exceedingly volatile, she said they were up 4.7% in July, down 2.3% in August and up 5% in September. Ms. Fink noted the source of the volatility was the market concern about how much the Fed would taper its bond purchases, known as quantitative easing. Ms. Fink attributed the strong returns in September to the Fed's surprise decision to maintain bond purchases at \$85B.

Ms. Fink also noted that in the quarter bonds fluctuated as well and ranged from as low as 2 1/2% to as high as 3% for the 10-year US Treasury. She said the overall portfolio was up 4.8% for the quarter with volatility of 7 1/2%.

Ms. Fink referenced a chart, which showed that ERSRI's portfolio showed similar or stronger returns and lower volatility than a basic 60% equity/40% bonds portfolio over a 3 and 5-year span. Mr. Licht then asked how the SIC measures volatility and Ms. Fink explained how the statistical measure of standard deviation is used to capture the variability in returns.

Ms. Fink explained why managing volatility is so important, using this example. If someone has a dollar and loses 50%, they have 50 cents. If they then gain 50% after that initial loss, they now have 75 cents. The average return of +50% and -50% is 0%, but the experienced return is -25%.

She pointed out that ERSRI's portfolio is designed to capture more of the upside and less of the downside from market moves, which played out in July, August, and September returns. Treasurer Raimondo then referenced an analysis Cheiron presented at a previous board meeting. It showed the cumulative impact from two different return profiles, one with a 7.8% average performance but volatile returns, and another with a consistent 7.5% each year. The one with 7.5% each year, she explained, ended with significantly more assets than the former.

Ms. Fink apprised the Board that the SIC has commissioned an asset allocation review and noted that it has been 2 1/2 years since the last asset liability study was done. Ms. Fink said that during this time, equity markets in the United States are up 40%, global equity markets up 25%, bonds up 10% with 10-year Treasury yields down from 3.3% to 2.5%. In this same period, Ms. Fink noted commodities and volatility have had sizable moves, so the SIC felt it was prudent to review the portfolio's asset allocation. Ms. Fink said PCA, the State's general investment consultant, will conduct the review.

Lastly, Ms. Fink said the SIC is working on creating a comprehensive investment policy statement. Treasurer Raimondo thanked Ms. Fink for her report.

IV. Executive Director's Report

Director Karpinski apprised the Board that they were in possession of the October 31, 2013 Pension Application Report, a presentation from Sullivan & Company, a division of Blum Shapiro, regarding the municipal audit and the Disability Subcommittee Report.

Director Karpinski noted for the Board that an email was sent to reschedule the December Board meeting to December 17, 2013 (Tuesday) since Gabriel, Roeder, Smith and Company (GRS), the system actuaries, were unavailable for the original Board meeting date. Director Karpinski noted that at the December 17, 2013 meeting, GRS would present the ERS and MERS valuations for approval. The Director then asked the Board for a motion to reschedule the December meeting.

On a motion by John P. Maguire and seconded by Gary R. Alger, Esq., it was unanimously

VOTED: To reschedule the December 11, 2013 Board meeting to December 17, 2013

The Director thanked the Board for their efforts at the October 21, 2013 planning session. He said it was a productive meeting and he would send information shortly to confirm the prioritized strategic goals and objectives.

The Director noted that the IT contractor, Morneau Shepell, is at ERSRI's office 3 days per week currently working on requirements gathering, pension payroll development and the accounting system requirements.

Director Karpinski apprised the Board regarding the status of the regulation regarding the *Social Security Option Adjustment*. He noted that there was a public hearing held on November 1, 2013 and no changes or comments were provided. Consequently, the regulation will become effective on November 24, 2013. The Director said an explanatory letter would be sent to the affected 1,200 members. Director Karpinski also informed the Board that Mr. Boudreau has been coordinating locations for providing a presentation to the affected members.

Director Karpinski then apprised the Board that the COMPASS newsletter will be mailed on November 22, 2013.

Director Karpinski noted for the Board that in the delinquency report of contributions in the Board book, the Town of North Kingstown had a recent transition in staff and their delinquency appeared to be a resource issue rather than a cash issue and ERSRI has been in contact with the Town Hall. In addition, Cumberland Rescue and the Town of Cumberland were noted as delinquent. The Director said if no funds are received by the end of the week, consistent with policy, an official letter would be sent to them requesting immediate payment of contributions.

Update on the Municipal Employer Payroll Audit by Blum Shapiro

Director Karpinski introduced Messer's, Michael Hanna, CPA and Michael Ferri, CPA of Sullivan & Company, a division of Blum Shapiro, to provide an update on the municipal audit.

Mr. Ferri began the presentation and said they have gone through 71 of the 187 business units managed by ERSRI. He said there is an eight-person rotating engagement team. He apprised the Board that the agreed upon procedures of the audit include a test of participants' compensation and contributions; transmission testing for compliance with ERSRI policies and Rhode Island General Law (RIGL); Non-member testing and Retired employee testing (post-retirement employment).

Mr. Ferri said the team is reviewing the collective bargaining agreements (CBA) within each of the bargaining units and cross-referencing it with the applicable RIGL. He also noted that within each business unit the team is performing a test on 10% of the population. He noted that 10% testing is quite high in performing audit testing. He apprised the Board of the following procedures:

- 1) Compare the actual employee contribution to the calculated employee contribution based on the pensionable compensation for the fiscal year ended June 30, 2012.
- 2) Compare the actual employer contribution to the calculated employer contribution based on the pensionable compensation for the fiscal year ended June 30, 2012.
- 3) Compare the employee and employer contribution rates for the fiscal year ended June 30, 2012 to the authorized rates under ERSRI policies.
- 4) Review the calculated pensionable compensation for the fiscal year ended June 30, 2012 to ensure that it includes income in compliance with ERSRI policies and the applicable Rhode Island General Laws.
- 5) Review the income excluded from the pensionable compensation calculation for the fiscal year ended June 30, 2012 to determine that it was properly excluded.

Mr. Ferri reiterated that they tested 71 out of 187 business units to date that totaled 9,338 total participants. He said of the population, they tested a sample of 1,059 participants and had a net understatement of employer and employee contributions of

\$15,248 and \$24,294, respectively. Mr. Hana said these results were elevated more than would have been preferred; however, two units made up the vast majority of the understatement variances, namely, Central Falls and North Kingstown. By removing the two isolated instances, the net understatement for participants tested was \$2,351 and \$2,223 for employee and employer contributions, respectively. Mr. Ferri noted that the misstatements were not seen as systemic and not necessarily a pattern amongst the units.

In summary, Mr. Ferri said the total understatement/overstatement of contributions, outside of isolated instances in Central Falls and North Kingstown, is very low. He said it is a testament to the staff within each of the towns and to the ERSRI staff that the understatement/overstatement is not greater given the complexity.

Mr. Ferri apprised the Board on the Central Falls' findings and said it related to longevity pay for the non-certified employees in the school department that resulted in a 40% error rate. Mr. Ferri said they found a total of 100 non-certified participants who should have been paid longevity and found 43 of the 100 did not have the contribution deducted resulting in a \$5,146 misstatement from employees and \$6,903 from the employer.

The other issue relative to the net understatement was North Kingstown Firefighters. Inadvertently, certain members who reached 30 years of service no longer had deductions remitted. Three members had not contributed amounting to an understatement of employee contributions of \$7,751 and employer contributions of \$15,168.

Mr. Ferri then discussed post-retirement employment and said the testing through October 15, 2013 identified 488 retired employees receiving benefits who are currently employed in the 71 business units tested. Testing confirmed that 11 members have worked over the maximum number of days allowed under RIGL. He said it remains a possibility that there could be more overages due to incomplete record keeping at the business unit level as well as the failure to submit "*Monthly Notification of Post Retirement Employment*" forms by the retiree. He noted that this test was one of the hardest tests to handle and is an area to consider improvement.

Mr. Ferri said that testing will continue and ERSRI will be made aware of any issues. Mr. Hanna said overall based on Blum Shapiro's testing, they were very comfortable on performed procedures and the error rate not including the Central Falls and North Kingstown issues.

Mr. Licht asked if prior years would be looked at relative to the Central Falls and North Kingstown issues. Director Karpinski said Central Falls has already been contacted and he will look at prior years.

The Treasurer thanked Messer's Hana and Ferri for their presentation.

Review and Potential Approval of Actuarial Valuation for Judges, Engaged Before December 31, 1989, as of June 30, 2012

Director Karpinski contacted Mr. Joseph Newton of Gabriel, Roeder, Smith and Company via conference phone. He apprised the Board that in the Board book there are two valuations, one assuming a pay-as-you-go financing and another assuming advance funding. Director Karpinski said Rhode Island has been positively noted for making required contributions on a consistent basis over the last 20 years, thus, recommended that the Board consider approval of the advance funding valuation. The Director said it would be prudent to make contributions that would result in taking advantage of

investment income to help reduce future contributions and additionally provide some security for those members included in the Trust. Director Karpinski asked Mr. Newton if he had any comments to offer the board. Mr. Newton said the Director provided a concise analysis of the valuations to the Board but said to use the advance-funded valuation in disclosures would mean the State would then have to begin actually funding the plan, which would have to be contributed before the fiscal year but not necessarily added in the current year.

Mr. Mullaney asked what the difference was between the two valuations since both have an Annual Required Contribution (ARC). Mr. Newton said the difference is that in the advance-funded valuation, the assumption is the accumulation of assets that would create investment earnings that would help to pay benefits in the future. Thus, he said the Trust may use a higher investment earning assumption, which would be consistent with the rest of the Trust fund at 7½%. Additionally, with the advance funding valuation, the ARC is the funding requirement, which becomes both the accounting number and funding number.

Mr. Newton then said with the pay-as-you-go valuation there are no asset accumulations to earn investment income; hence, the actuarial and accounting standard dictates the use of a lower discount rate thus incurring a higher liability.

Mr. Licht asked Mr. Newton how he calculated the expected benefit payments with a size of seven members. Mr. Newton said he used the same methodology used in the other plans where certain probabilities and percentage of retirement is computed. He noted when the next valuation is performed and no retirements occur, a slight gain would develop in the liability but the benefits for those members may be higher.

Mr. Licht asked Mr. Newton if there has ever been an experience study on the contributing Judges' plan and he said no since there is not enough data for retirement analysis. Director Karpinski noted that there are 44 judges in the contributory plan. Mr. Licht felt that doing an assumption on only seven people was statistically difficult and less reliable.

Mr. Licht asked if Mr. Newton combined the seven Judges with the 44 who are in the contributory plan, in an effort to have a larger sample size, would the ARC have risen to the same amount. Mr. Newton said they would not change the assumptions but could change the methods with a little more flexibility in the amortization schedule.

Treasurer Raimondo said a trust has been set up so the State should pay the employer contribution into the Trust as it does with all the other Trusts that are established. The Treasurer concurred with both Director Karpinski and Mr. Newton on the analysis regarding being prudent and making contributions, which would result in taking advantage of investment income to help reduce future contributions and provide some cushion of security for those included in the Trust.

Treasurer Raimondo asked for a motion to approve the advance-funded valuation but would open the vote for the Board's opinion. She also said that approving a valuation would avoid a qualified opinion from the Auditor General.

Mr. Maguire asked Mr. Newton what is the advantage of one plan over the other. Mr. Newton said putting in more money now protects the members if there was some negative scenario. He said if you use the "pay-as-you go" method, there is only the full faith of the State to make pension payments.

Treasurer Raimondo said as the Board are the fiduciaries, it is incumbent on them to be concerned about the health and funding of the Trust and to fund it properly. However,

the Treasurer said the General Assembly, because of budget issues, could choose not to act on the advance funding valuation if approved. Director Karpinski said if that were the case, Mr. Newton would have to use the pay-go method in the next valuation cycle thus lowering the discount rate.

A motion was then made by Richard A. Licht and seconded by Thomas A. Mullaney to accept the Actuarial Valuation for Non-contributing Judges as of June 30, 2012, assuming pay-as-you-go financing. A roll call was taken, and the following members voted Yea: Vice Chair William B. Finelli, Michael R. Boyce, Richard A. Licht, John P. Maguire, and Thomas A. Mullaney. The following voted Nay: General Treasurer Gina M. Raimondo; Gary R. Alger, Esq.; Daniel L. Beardsley; Frank R. Benell, Jr.; M. Carl Heintzelman; John J. Meehan; Claire M. Newell and Jean Rondeau.

There being 13 votes cast, 5 voted in the affirmative and 8 nay, consistent with Rhode Island General Laws 36-8-6, *Votes of the Board – Record of Proceedings*, there being a majority vote of the members present and voting at which a quorum was present, the motion failed.

A motion was then made by Gary R. Alger, Esq. and seconded by Jean Rondeau to accept the Actuarial Valuation for Non-contributing Judges as of June 30, 2012, assuming Advance Funding. A roll call was taken, and the following members voted Yea: General Treasurer Gina M. Raimondo; Vice Chair William B. Finelli, Gary R. Alger, Esq.; Daniel L. Beardsley; Frank R. Benell, Jr.; Michael R. Boyce; M. Carl Heintzelman; John P. Maguire, John J. Meehan; Claire M. Newell and Jean Rondeau. The following voted Nay: Richard A. Licht and Thomas A. Mullaney.

There being 13 votes cast, 11 voted in the affirmative and 2 nay, consistent with Rhode Island General Laws 36-8-6, *Votes of the Board – Record of Proceedings*, there being a majority vote of the members present and voting at which a quorum was present, it was then

VOTED: To accept the Actuarial Valuation for Non-contributing Judges as of June 30, 2012, Assuming Advance Funding.

Mr. Maguire inquired of Mr. Newton about a group of retired state troopers that are also not part of a Trust and asked whether there would be a similar study for this group. Mr. Newton said no as no trust has been established and there are no contributions required of active troopers at this time who are pay-as-you-go.

V. Administrative Decisions

None this month

VI. Approval of the October Pensions as Presented by ERSRI

On a motion by John P. Maguire and seconded by Jean Rondeau, it was unanimously

VOTED: To approve the October pensions as presented.

VII. Legal Counsel Report

Attorney Robinson suggested that a motion would be in order for the Board to convene in Executive Session to discuss the three pending litigation matters identified on the

agenda pursuant to Rhode Island General Laws section §42-46-5 (a)(2) regarding pending or potential litigation involving the Retirement System.

Consistent with Rhode Island General Laws section §42-46-5 (a)(2) regarding pending or potential litigation involving the Retirement System, a motion was made by Daniel L. Beardsley and seconded by John P. Maguire to convene the Board in Executive Session to discuss the identified litigation matters involving the Board.

A roll call vote was taken to enter into Executive Session, the following members were present and voted Yea: Vice Chair William B. Finelli; Gary R. Alger, Esq.; Daniel L. Beardsley; Frank R. Benell, Jr.; Michael R. Boyce; M. Carl Heintzelman; John P. Maguire; John J. Meehan; Thomas A. Mullaney; Claire M. Newell and Jean Rondeau. It was unanimously

VOTED: To convene the Board in Executive Session pursuant to Rhode Island General Laws section §42-46-5 (a) (2) to discuss the identified litigation matters involving the Board.

[Executive Session]

The Board thereafter convened in executive session.

Treasurer Raimondo and Richard A. Licht entered the room after the roll call and the Board was in executive session.

[Return to Open Session]

Upon returning to open session, the Board noted for the record that the following votes had been taken in executive session:

The Board authorized Board Counsel Michael P. Robinson to represent both General Treasurer Gina M. Raimondo and Executive Director Frank J. Karpinski in their official and individual capacities in the matter of *Michael T. Brady vs. Gina M. Raimondo et al.* A motion was made by Jean Rondeau and seconded by Richard A. Licht, it was

VOTED: To authorize Board Counsel Michael P Robinson, Esq. to represent General Treasurer Gina M. Raimondo and Executive Director Frank J. Karpinski in both their official and individual capacities in the matter of *Michael T. Brady vs. Gina M. Raimondo et al.*

The Treasurer abstained from the vote and the vote was unanimous.

Lastly, on a motion made by William B. Finelli and seconded by John P. Maguire, to exit executive session and return to open session, it was unanimously

VOTED: To exit executive session and return to open session.

VIII. Committee Reports

Disability Subcommittee:

The Disability Subcommittee recommended the following actions on disability applications for approval by the full Board as a result of its meeting on November 8, 2013:

Name	Membership Group	Type	Action
1. Lauren Vierra	Teacher	Deny -- Accidental	Approve -- Ordinary
2. Henry Jacques	State	50% -- Accidental	Approve
3. Mark Hanlon	State	50% -- Accidental	Approve
4. David Palumbo	State	Accidental	Postpone
5. Linda Acciardo	State	Accidental	Deny
6. Nicholas Romeo	Municipal	Accidental	Postpone
7. Paul Venditto	Municipal	Accidental	Approve
8. Alan Purtee	State	Accidental	Approve @ 50%
9. Christopher Leveillee	Municipal	Deny -- Accidental	Approve -- Ordinary
10. Keith Printer	Municipal	Accidental	Deny
11. Philip Brodeur	State	Ordinary	Approve
12. David Fournier, Sr.	State	Ordinary	Approve
13. Harry Coli, Jr.	State	Accidental	Approve
14. Richard Saborio	Teacher	Accidental	Approve

On a motion by William B. Finelli and seconded by Michael R. Boyce, it was unanimously

VOTED: To approve the recommendation of the Disability Subcommittee meeting of Friday, November 8, 2013 on items 1-14.

IX. Adjournment

There being no other business to come before the Board, on a motion by William B. Finelli and seconded by Richard A. Licht, the meeting adjourned at 10:43 a.m.

Respectfully submitted,

Frank J. Karpinski
Executive Director